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UNCLAS SECTION 01 OF 02 ANKARA 000446

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SUBJECT: "2005-YEAR OF PRIVATIZATIONS?"

REF: ANKARA 06963

1. (U) Summary: Vice President of the Privatization Administration (PA), Hasan Koktas, told us he is bullish on Turkey's privatization prospects for 2005 noting Turkey's favorable market conditions. Koktas is in charge of several of the GOT's largest pending privatizations: the tobacco division of Tekel; the state oil refining company, Tupras; and the massive steel corporation, Erdemir. If the PA can pull off one or two of its planned large privatizations in 2005, it will help restore the credibility of the program. End Summary.

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Privatizing Portfolio of Large Companies  
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2. (U) Koktas told econoffs that while the PA has succeeded in privatizing most of the state's small and medium-sized companies, it is hoping to privatize 3 to 5 of the state's largest companies this year. Koktas is in charge of some of the most ambitious privatization projects slated for 2005, including: the tobacco division of Tekel; the state oil refining company, Tupras; and the steel corporation, Erdemir. Though not under Koktas' responsibility, the PA also plans to tender telecom parastatal Turk Telecom in 2005 and to try again to sell the petrochemical company, Petkim. Having succeeded in selling much of its portfolio of small companies, Koktas claimed that the PA is ready to move to market the large state-owned companies. He pointed out that there is not enough domestic capital to support the privatization of some of the larger companies--making international interest from "strategic investors" critical. Koktas was hopeful that a good economic outlook, EU accession, and favorable global market conditions will facilitate this.

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Plans for Three Giants: Tekel, Tupras, and Erdemir  
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3. (U) Koktas shared with econoffs the PA's privatization timeline and plans for Tekel, Tupras, and Erdemir:

--Tekel: 4 or 5 companies are interested in the tobacco operations of Tekel. The PA expects to receive the first round of bids on February 18. Japan Tobacco International (JIT) and British American Tobacco are two interested companies which purchased tender documents. (Though Koktas claimed that Phillip Morris was still undecided on whether or not it would bid, press reports indicate that competition barriers would more than likely exclude Phillip Morris from bidding.) Note: In 2003, JIT's \$1.3 billion bid was rejected as too low. End Note.

--Tupras: The PA expects to launch a tender announcement for Tupras during the first week of April. Though the last attempt to sell 65% of the company was blocked by legal challenges, Koktas is confident the next attempt will be more successful. He thought that expected changes in the Privatization Administration basic law being debated in Parliament would reduce the grounds for legal challenges. The PA is contemplating selling 51% of the company in a block sale and 14% through Initial Public Offerings (IPOs). Koktas also emphasized the need for greater interest from international investors, particularly from the U.S. and western Europe. He noted that mainly Russian companies had shown serious interest in Tupras previously.

--Erdemir: As one of the biggest companies in Turkey, Koktas said that a successful sale of the Erdemir steel corporation would be a significant achievement in the GOT's privatization efforts. Currently, 51% of the company is publicly owned and traded on the Istanbul stock exchange. Erdemir itself owns 2.9% of the company. The PA plans to sell its 46.12% of the total capital of the company. Along with the 2.9% this would ultimately give the buyer the ability to have control of the company if it buys an additional 1.1% from the stock exchange. The PA plans to lift the "golden share" condition in order to comply with EU principles. The announcement for

the sale is scheduled for mid-March. Note: Erdemir has been profitable in 2004 and 2003, as Turkey's auto and white goods boom has accelerated demand for steel. U.S. Steel has expressed strong interest in Erdemir (ref), which is welcomed by Turkish officials at all levels. End Note.

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The Tender Process  
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14. (U) Econoffs asked Koktas if price alone was the main factor in evaluating bids and Koktas said it depended on the company. For Erdemir, for example, the PA looks at 2 pre-qualifications--one being financial and the other operational. Before analyzing the pre-qualifications of the company, the PA usually takes 5 months to prepare the tender document followed by 2 months of due diligence. The PA then obtains bids and analyzes the business plans--be it employment or expansion plans or projections-- as well as the pre-qualifications of the companies. The PA then opens the companies' "price envelopes" and prepares a short list of companies to participate in the auction process. The results of the tender process are sent to the Competition Authority for approval and subsequently to the Privatization High Council.

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Legal Obstacles to Privatization  
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15. (SBU) The PA's last successful sale involving a large parastatal, was the sale of a minority share of Turkish Airlines (THY) through an IPO. But Koktas believes any future big sales for Turkey will require greater interest from strategic investors. He claims, however, that the current Turkish legal system presents major obstacles to Turkish privatization and hampers foreign direct investment (FDI) as evinced in the previous failed attempt to sell Tupras. Koktas said that Turkish judges have an ideological view of privatization rather than judging transactions on their legal merits. Koktas told econoffs that a new draft of the PA law will go to Parliament shortly--amending one of the law's articles to ensure that any future suits are sent to the high courts and not local courts which might take a parochial view of privatization.

16. (SBU) Comment: If the PA succeeds in several of its planned privatizations as described above, 2005 will be a blockbuster year for GOT privatization. However, if the GOT continues, as it has in the past, to focus primarily on price as the key criteria for a successful bid and if it does not resolve labor grievances before they escalate in the Turkish court system, then 2005 may not produce the big ticket sales the PA is promising. If, on the other hand, the PA is successful with even one or two big privatizations, it will revive the battered credibility of the program, encourage Foreign Direct Investment, and help finance the current account deficit. End Comment.

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